

A PRIMER FOR U.S. ASSET MANAGERS:

Exploring New Permanent Capital Opportunities

Finding Success in the London-Listed Fund Market

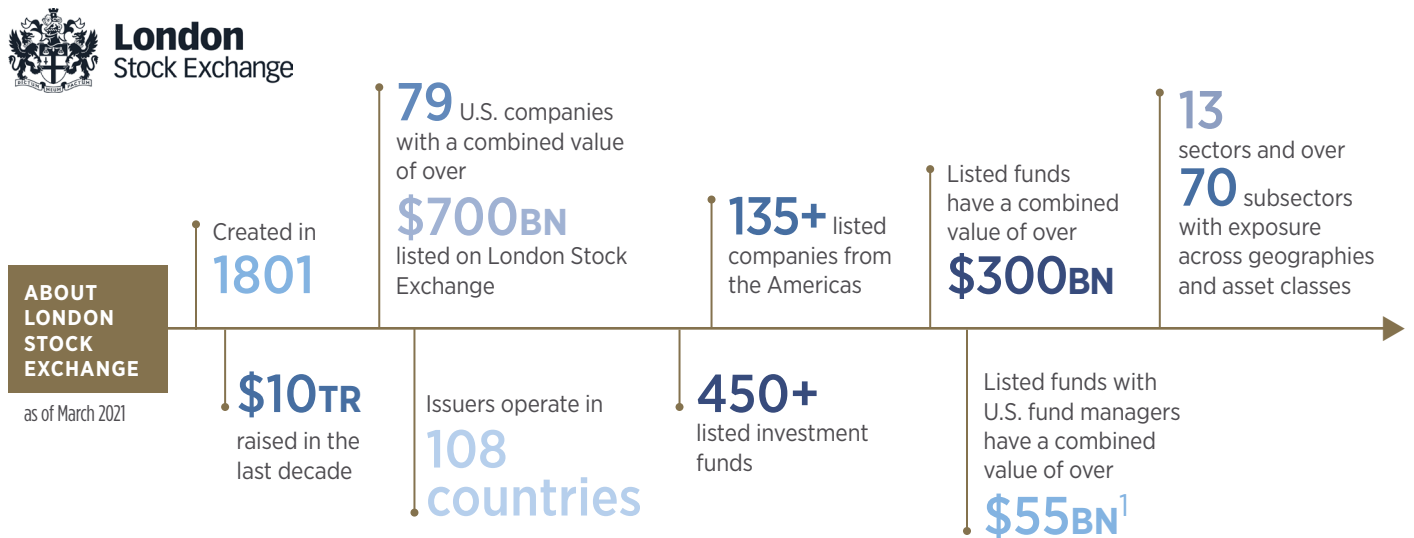




London Stock Exchange is the most venerable market in the world for publicly traded closed-end investment companies, known in the U.K. as investment trusts.

F&C Investment Trust was the first such closed-end fund (CEF) to launch in London in 1868 and is still listed today. The London-listed investment trust sector is large, with a market cap of approximately \$300 billion. To understand why U.S.-based managers are increasingly turning to London Stock Exchange—and whether London is a good fit for a particular manager or strategy—it is important to look at some of the key distinctions between the U.K. and U.S. listed investment fund markets.

There are advantages—and disadvantages—of launching a listed fund in London instead of New York. It is clear that any U.S. manager considering a London listing will need partners with structuring expertise in both markets. Perhaps more critical, albeit more subtle, is finding a partner with the ability to understand as well as anticipate the investment appetite in the U.K. market.



¹ This figure includes both investment trusts with fund managers based in the U.S. and those with fund managers that have U.S.-based parent companies. London Stock Exchange only recognizes investment trusts with fund managers based in the U.S. as funds with U.S. managers (about \$19.4bn in combined value).

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U.S. Managers May Benefit from Launching in London

“The regulatory structure in London offers more flexibility on diversification, liquidity, leverage, and more... And also in terms of cost, it's typically less expensive for funds to raise capital in London versus the U.S.”

Wendy Huang

Business Development Manager,
Primary Markets, London Stock
Exchange Group, May 2021

London-listed investment trusts offer access to a different investor base than U.S.-listed funds. The London market is dominated by sophisticated institutional investors at launch, many of whom have a specific investment trust mandate. The majority of investment trusts list on the Premium Segment of the Main Market, which offers access to the British retail market in addition to institutional investors¹, allows index inclusion and has a minimum free float of 25%. London-listed investment trusts with more complex capital structures, security types or investment policies may list on the Specialist Fund Segment (SFS) of London Stock Exchange's Main Market, which has no perspective free float requirement and a professional investor base.

Unlike U.S. listed CEFs, London-listed investment trusts are not governed by the Investment Company Act of 1940.² In practical terms, this means managers can charge performance fees and have greater flexibility in how to use leverage. Additionally, test marketing in advance of launch is a best practice (and legal), to get an indication of market appetite for a fund. This marketing period may occur simultaneously with regulatory approval processes, allowing managers to launch investment trusts in as little as four months after the first kick-off meeting. Follow-on capital raising is common, sometimes taking place shortly after the launch. The following table provides an overview of additional similarities and differences between London-listed investment trusts and U.S. listed CEFs.

Comparison of U.S. and U.K. Listed Investment Fund Structures

	U.S. Listed CEFs	U.K. Investment Trusts
Asset Pools	Permanent capital (if perpetual) Long-term capital (12-year term)	Permanent capital
Liquidity	Exchange listed	Exchange listed
Investor Base at Launch	Retail, broad base	Institutional, smaller base
Number of Investors on IPO	2,000–15,000	50–150
Typical Strategy Objective	Income: 5–7% income yield	Income: 5.5%+ income yield; Growth: 0% income yield acceptable for select venture capital and private equity strategies
IPO Size	\$200mm–2bn	\$150–450mm; £100–350mm
Follow-On Offerings	Less common: Shelf registration for an at-the-market (ATM) program can be established after one year. ATM issuance occurs only if fund trades at a premium to net asset value (NAV).	Common: Follow-ons can commence shortly after IPO and continue as long as fund trades at NAV or a premium and investor demand exists.

Source: XA Investments

Key features of a London-listed investment trust

- Long-term investment horizon
- Relatively long initial term³
- Alternative strategies
- Institutional investor base
- Leverage
- Performance fees are possible
- Pre-marketing permitted
- Capped issuance costs⁴
- Independent Board of Directors

The strategies featured in recently launched London-listed investment trusts also differ from those typically housed in U.S. listed CEFs. With a focus on alternatives and environmental, social and governance (ESG) strategies, the U.K. market is very responsive to new investment trends. And although large sponsors routinely launch funds, the U.K. market is also open to new managers who have never listed a fund before. The average size of an IPO on London Stock Exchange is \$150 to \$450 million, effectively creating a lower bar to entry compared to the mega launches in the U.S. The London market also has a wider pool of brokers than the handful dominating the U.S. market, reducing a potential chokepoint.

However, listing a London investment trust can be challenging as well. U.K. investor preferences may change based on performance and market factors, and an investment strategy may fall out of favor with the U.K. market before a manager is able to launch a listed investment trust. Additionally, U.S. managers considering listing on London Stock Exchange may be unfamiliar with the regulations applicable to U.K. investment trusts. The London based advisory community is used to working with managers who are new to the market.

¹ Investment trusts on London Stock Exchange may be eligible to list on the Premium Segment of its Main Market, the Specialist Fund Segment (SFS) of its Main Market or the growth market AIM. Please see the glossary for more information on each market. ² Each London Stock Exchange market has its own level of regulation regarding listed investment trusts. ³ Management agreement terminable typically on 12 months notice after expiry of a relatively long initial fixed term. ⁴ The issuance costs that investors will bear are generally capped at 2% of gross proceeds, but these costs may vary between offerings.

London-Listed Investment Trust Launch Potential Criteria

When determining which strategies are appropriate for a London-listed investment trust, managers may consider the following criteria.

Strategies that are <i>likely</i> to attract institutional investors in the London-listed investment trust marketplace	
Income	Current yield of 5.5%+ to attract institutional investors who are seeking income
Private Markets	Less liquid or illiquid investments in private markets are favored over publicly traded securities
Alternatives	Investors look to closed-end investment trusts to house uncorrelated illiquid assets (e.g., green infrastructure, real estate, digital infrastructure, etc.)
Premiums	Similar strategies to competitor funds that currently trade at premiums
ESG/Impact	Funds investing in ESG/sustainable strategies have been embraced by the market in recent years
New/Niche	New asset classes can be created in specialty focus areas (e.g., song royalties, aircraft, etc.)
U.K. Focus	Demonstrate some affinity or benefit for the U.K. (e.g., Home REIT that provides housing for U.K. homeless population)
U.S. Manager	Known, respected manager will increase chances of success in marketing
Seed Capital	Many offerings have seed capital or an existing pipeline, invest-up runs 6-12 months (12 month maximum)
Strategies that are <i>less likely</i> to attract institutional investors in the London-listed investment trust marketplace	
Growth	Diversified private equity strategies or fund-of-fund private equity may be difficult to launch due to the lack of current yield. Exceptions apply for niche sector-focused private equity or venture capital strategies
Public Securities	Investors do not look to closed-end investment trusts to house traditional assets that they can access directly (e.g., public equities)
Discounts	Similar strategies to competitor funds that currently trade at discounts are less likely to succeed. Use pre-marketing period to gauge current investor sentiment

Source: XA Investments

A number of U.S.-based managers have had success launching investment trusts in London in recent years, as shown in the table below. London clearly is not the right fit for every manager or strategy. Perhaps the most significant barrier to more U.S. managers (including those considering listing existing interval funds) launching investment trusts on London Stock Exchange might simply be lack of awareness of the opportunities.

Examples of U.S. Asset Managers that have listed funds on London Stock Exchange

	Round Hill Music Royalty Fund	Marble Point Loan Financing	VPC Specialty Lending Investments	Blackstone/GSO Loan Financing
Adviser	Round Hill Music	Marble Point Credit Management	Victory Park Capital Advisors	Blackstone/GSO
Firm Inception	2010	2016	2007	1985
Firm Headquarters	New York, NY	Greenwich, CT	Chicago, IL	New York, NY
Ticker	RHM	MPLF	VSL	BGLF
Fund Launch Date	13 November 2020	13 February 2018	17 March 2015	23 July 2014
Strategy	Music royalties	Collateralized loan obligation (CLO) debt and equity	Direct lending	Senior secured loans and CLO debt and equity
Main Market Segment	SFS	SFS	Premium	Premium
Capital Raised at IPO	\$282 million	\$43 million	\$295 million	\$350 million
AUM (as of 1 Feb 2021)	\$319.8 million	\$148.8 million	\$404.3 million	\$494.9 million
Why Unique	First (and only) music royalties fund listed on London Stock Exchange by a U.S. manager Second music royalties fund after Hipgnosis Songs Fund (LSE:SONG), launched in 2018 (\$1.81 billion AUM as of 1 Feb 21)	Marble Point and the fund are sponsored by Eagle Point Credit Management, the adviser to Eagle Point Credit Company (NYSE:ECC), one of the few CLO-focused listed CEFs in the U.S.	VPC Specialty Lending Investments represents the first (and only) listed fund launched by Victory Park in either the U.K. or the U.S.	Blackstone had already launched three U.S. CEFs before deciding to launch a London-listed fund

Source: The Association of Investment Companies (AIC), theaic.co.uk

State of the London Listed Market in 2021

“The pre-marketing process with U.K. institutional investors gives fund managers the confidence they need to proceed to fund launch without significant outlays of time or expense. Once the decision to proceed is taken, pre-marketing continues in parallel with confidential prospectus filings with the regulator. This enables the IPO process to be concluded relatively quickly—as little as four months from kick-off meeting to the shares trading may be achievable with a fair wind.”

Nigel Farr

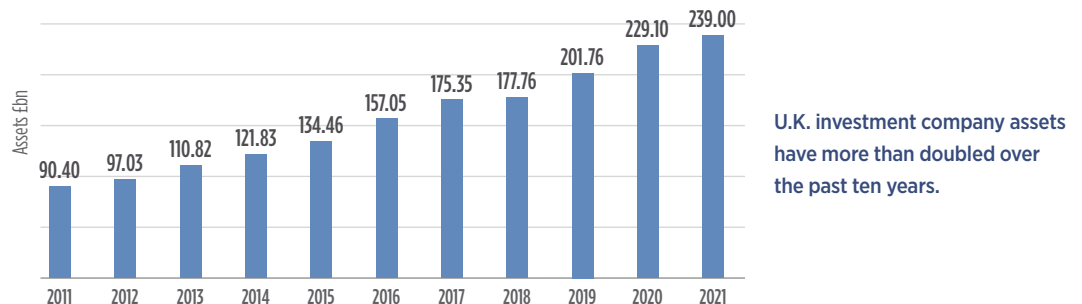
*Partner, Herbert Smith Freehills,
May 2021*

The U.K. investment trust sector benefits from a broad investor base encompassing such institutional investors as discretionary fund managers and wealth managers, in addition to funds of funds and substantial retail support (with an increased number of investment platforms offering retail investors access to investment trusts). As such, there is a tendency for investors to look to the investment trust sector to complement the opportunities available in the equity market. Given its relatively flexible regulatory framework, low costs to entry and sophisticated investor community, the U.K. market is quick to respond to developing investment trends and tends to see more niche, differentiated strategies come to market than the U.S. listed fund space.

More recently, many new London-listed investment trusts have focused on ESG factors. 2020 marked the third consecutive year with three renewable energy infrastructure fund IPOs, as well as London Stock Exchange’s first diversified social impact fund and a REIT focused on providing accommodations to the homeless. In addition, two of the largest four follow-on offerings in 2020 were by renewable energy infrastructure-focused funds.

The secondary trading market for U.K. investment trusts reflects global investment themes expressed by such funds as growth equity (Scottish Mortgage at \$25bn market capitalization, the largest outside investor in Tesla), emerging markets (Fidelity China Special Situations at \$3.5bn market capitalization) and market disruption (hedge fund Pershing Square at \$9.5bn market capitalization). With respect to more established investment trends in the London-listed investment trust market, we see the continued demand for funds with attractive income levels. There is also demand for infrastructure-focused private investments. Emerging trends in life sciences investments and inflation-protected income-producing investments stem from the response to the COVID-19 pandemic.

U.K. Investment Company Industrywide Assets



Source: AIC/Morningstar, as of 3/31/2021

A Global Opportunity

U.S. asset managers interested in permanent capital vehicles and seeking ways to diversify their investor base should consider the London-listed investment trust marketplace. The institutional investor base in London is open to both boutique and well-established asset managers that have a demonstrated track record of success in less liquid or illiquid investment strategies. In the low interest rate environment, London-listed investment trusts that produce attractive levels of income are especially well received. Please let us know if you would like to learn more about opportunities for capital raising in the London market.

Glossary

For purposes of this publication, terms are defined below.

AIM is London Stock Exchange's market for small and medium size growth companies in need of access to capital, providing companies with access to a diverse set of investors and a supportive advisory community, who understand the needs of entrepreneurial businesses.

At-the-market (ATM) is an offering of shares pursuant to a shelf registration statement into an existing trading market for outstanding shares of the same class, at prices based on the price of the outstanding shares in the trading market. Essentially, a U.S. listed CEF may offer new shares at the current market prices for its shares, as long as such prices are at a premium to the CEF's current net asset value.

ESG (Environmental, Social, Governance), and often used to describe the consideration of these three factors when selecting investments.

Exchange listed describes companies, including listed investment funds, that are traded on a stock exchange.

Free float refers to shares held in public hands. This excludes, for example, shares held by significant shareholders and company directors.

FTSE Russell is a subsidiary of London Stock Exchange Group that is a leading global provider of financial indexing, benchmarking and analytic services with more than \$16 trillion benchmarked to its indices.

Investment Company Act of 1940 regulates the organization and oversight of U.S. investment funds, including mutual funds and closed-end funds, that engage primarily in investing, reinvesting, and trading in securities, and whose own securities are offered to the investing public.

IPO initial public offering

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Liquidity is the degree to which an asset or security can be bought or sold easily without the transaction affecting the asset's price.

Premium Segment is London Stock Exchange's Main Market segment dedicated to equity shares issued by trading companies and investment entities. Premium-listed companies are required to comply with the U.K.'s highest standards of regulation and corporate governance. By virtue of these higher standards, companies and funds may qualify for inclusion in the FTSE UK Index series and enjoy access to a broader range of investors. Funds listed on the Premium Segment can access both retail and institutional investors.

Specialist Fund Segment (SFS) is London Stock Exchange's dedicated Main Market segment for specialist, closed-ended investment funds targeting institutional, professional, professionally advised and knowledgeable investors. Types of fund investments include private equity, feeder funds, hedge funds, specialist geographical, sophisticated structures of security types, specialist property, infrastructure, sovereign wealth and single asset funds.

A **U.S. listed CEF** is a traditional listed closed-end fund, which is an actively managed portfolio of pooled assets that raises a fixed amount of capital through an initial public offering (IPO) and then is listed on a stock exchange. Listed CEFs do not continuously offer or redeem shares directly to and from investors (with certain exceptions). Listed CEF shares trade like an equity, with prices that fluctuate throughout the business day.

A **U.K. investment trust**, also known as a "listed investment fund," is an actively managed, closed-end investment company, with shares listed and available for trading on London Stock Exchange. Listed investment trusts do not continuously offer or redeem shares directly to and from investors (with certain exceptions). Listed investment trust shares trade like an equity, with prices that fluctuate throughout the business day.

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